

CHART K-6
HISTORY OF CALIFORNIA
GENERAL OBLIGATION BOND RATINGS
(1980 TO 2000)

The following reflects the years in which the State of California's bond ratings were changed, including a summary of the rating agency rationale for the changes:

- 1980** **Moody's** downgraded from Aaa to Aa, and **S&P** from AAA to AA+. Actions were attributed to uncertainty over impact of Proposition 13 and the Gann spending limit on state finances in light of the national economic slowdown.
- 1983** **S&P** downgraded to AA. Action coincided with California's first issuance of revenue anticipation notes (RANs) in January 1983, which were issued to, in part, redeem \$400 million in warrants issued in November 1982. California had been placed on CreditWatch by **S&P** in October 1982, as a result of cash shortages which led to the issuance of the warrants.
- 1985** **S&P** upgraded to AA+ due to improved financial performance and cash position.
- 1986** **S&P** upgraded to AAA due to "strong outlook for economic base, strong financial management, commitments to addressing pension liabilities, and a strong financial base with good prospects for maintenance of prudent reserves."
- 1989** **Moody's** upgraded to Aaa, citing restoration of adequate fund balance in the reserve for economic uncertainty and the state's economic strength and diversity.
- 1991/92** Ratings lowered by **all three agencies** due to state's fiscal condition and heavy reliance on external borrowing.
- 1994** **S&P** lowered to A, citing the state's continuing deferral of substantial portions of its estimated \$3.8 billion accumulated deficit, including off-book "loans" to schools; continuing structural budgetary constraints including Proposition 98's funding guarantee for K-14 education; overly optimistic expectations of federal aid to balance the 1994-95 budget and the 1995-96 cash flow projections; and its reliance upon a blunt trigger mechanism to reduce spending if the assumptions prove to be inflated.
- Moody's** lowered to A1, citing the state's heavy reliance on the short-term note market to finance its cash imbalances, and the likelihood that this exposure will persist for at least two years. Moreover, the constraints imposed by voter initiative and the political environment are likely to cause

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fiscal stress to persist after the accumulated deficit is finally extinguished, given an expected backdrop of only moderate economic growth and growing demographic pressures. **Fitch** lowered rating to A.

1996 **Fitch** upgraded to A+, citing the elimination of the deficit, an improved cash position, and good prospects for growth. Still there are long-term problems from the restrictions imposed by restructuring initiatives, including mandating of strict property tax limits and the share of the budget which must be devoted to education as well as uncertainties which necessarily accompany an economy in transition.

S&P upgraded to A+, citing broad economic improvement, the stabilization of aerospace employment, improved liquidity position, including the end of borrowing across fiscal years, and more realistic budget assumptions. S&P also cites structural budget impediments, such as mandated school funding levels, tough new mandatory sentencing laws, and a two-thirds legislative vote for budget passage, as contributors to the single A+ rating. S&P indicated that absent significant structural change in budgetary constraints, it is unlikely to further raise the state rating.

1997 **Fitch** upgraded to AA-, citing California's improving economy and favorable outlook.

1998 **Moody's** upgraded to Aa3. The upgrade reflects the State's continuing economic recovery, coupled with a number of actions taken in the recent legislative budget session to improve the State's credit condition, including the rebuilding of cash and budget reserves. In addition, five-year financial projections indicate long-term budget balance can be maintained even under assumptions of slowing economic growth.

1999 **S&P** upgraded to AA-. The upgrade reflects California's strong economic performance and a return to structural fiscal balance as demonstrated by: a positive GAAP General Fund balance for fiscal year 1997-98, a continued positive budgetary basis fund balance at the end of fiscal year 1998-99 and conservative budgeting in the adoption of the 1999-00 Budget.

2000 **Fitch** upgraded to AA. The upgrade takes into account the fundamental strengths of California, buttressed by the sustained favorable economy and financial operations. The General Fund had a substantial balance at June, 30 1999, and revenues to date this year are well above estimates, pointing to another successful year. The proposed budget for 2000-01 is based on conservative expectations and includes a good level of reserves.